

BEFORE THE  
POSTAL RATE COMMISSION  
WASHINGTON, D.C. 202268-0001

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POSTAL RATE AND FEE CHANGES, 2000:

Docket No. R2000-1

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**JOINT REPLY BRIEF**  
**OF**  
**AMERICAN BANKERS ASSOCIATION**  
**AND**  
**NATIONAL ASSOCIATION OF PRESORT MAILERS**  
  
**(September 22, 2000)**

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## **I. Introductory Statement**

The Commission's normally difficult task of recommending fair and equitable rates for scores of rate categories has been complicated in this case by multiple changes in the data on which a recommendation has to be based. As pointed out in ABA & NAPM's joint Initial Brief, the Postal Service made significant filings as late as August 25, 2000, which could affect the Commission's recommendation, many of which were not subject to the discovery process which has become essential in recent cases for separating good from bad USPS data. ABA and NAPM urge the Commission to avoid allowing the numerical cacophony present in the latter stages of this case to distract it from recognizing the increasing value of worksharing by First-Class mailers since R97-1, which is amply established by the record in this case.

Worksharing First-Class mailers, including the members of ABA & NAPM, have invested millions of dollars in automation equipment and facilities. These long term investments have been made in good faith on the expectation that worksharing mailers would share in the mail processing savings which their efforts have brought to the Postal Service. However, in this case, the Postal Service has continued to frustrate these expectations by trying to minimize measurements of the costs avoided by these efforts. For example, Postal Service witness Miller excluded 35 mail processing cost pools and \$1.5 billion of move update savings from his calculations of automated FCLM cost avoidance.

Changed methodologies and late-filed data make analysis difficult; but it is clear that if measured consistently and fairly, cost avoidance of workshared First-Class mail is rising and the Commission should recognize this by increasing First-Class

worksharing discounts as proposed by ABA & NAPM. These increased discounts would reflect both the true level of cost avoidance associated with workshared First-Class mail and the importance of this mail to the Postal Service. To cut the real value of First Class workshare discounts in this case in spite of such increasing cost avoidance would place a substantial chill on the growth of the worksharing program which is so important to the Postal Service.

**II. Reliance Upon Flawed FY 1999 CRA Cost Data Raises Substantial Due Process Concerns; Reliance Upon Postal Service August 25, 2000 Updated Library References Utilizing The 1998 IOCS Methodology To Measure Automated FCLM Cost Avoidance, Or Upon FY 2000 Cost Estimates As Suggested By OCA, Would Be The Straw Which Breaks The Back Of Due Process.**

ABA&NAPM noted in their Initial Brief significant due process concerns and related evidentiary flaws which have resulted from the effort to incorporate into this case FY 1999 CRA data, particularly as that data relates to measurement of automated FCLM cost avoidance. We recognize the value of relying upon more recent cost data; but we submit that the record only benefits from incorporation of such data when it can be incorporated in a fashion which allows full analysis of such data through normal discovery procedures. ABA&NAPM submit that the time constraints in this proceeding have prevented the Commission from incorporating the FY 1999 CRA data into the record in such a manner. Consequently the FY 1999 CRA data lack sufficient credibility to be relied upon by the Commission, particularly in the case of measurement of automated FCLM cost avoidance where, as explained below, significant cost data were

added in the form of updated Library References at an extremely late stage in the proceedings.

ABA&NAPM therefore agree with the Postal Service's characterization, as set forth in its Initial Brief, of the results of the Commission attempts to incorporate FY 1999 CRA data, including the following statements: <sup>1</sup>

"Attempts to create a new base year foundation for test year estimates have resulted in errors, gaps and due process concerns"

"One inevitable consequence of the complex updating process was to magnify the opportunities that errors will be created and go undetected."

"Given the stage of the proceedings at which the updated materials were prepared and filed, neither the Postal Service nor the parties have really had adequate time to review and digest all of the information. The problems described above are those that have managed to surface so far, it is likely there are others that remain undetected." (emphasis supplied)

"The Postal Service has concluded that the effort to replace the base year in this case has failed to create an appropriate foundation, either to evaluate the Postal Service's Request, or to afford parties, including the Postal Service, adequate due process in relation to the Postal Service's and other parties' proposals."

However, ABA&NAPM oppose the totally inconsistent position taken by the Postal Service in its Initial Brief with respect to reliance upon updated Library References LR-1-477 and 478, which were filed by the Postal Service on August 25, 2000 and which utilize the 1998 IOCS methodology to measure automated FCLM cost avoidance. In particular, the Postal Service states at Page VII-78 of its Initial Brief that although it

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<sup>1</sup> Postal Service Initial Brief, R2000-1, at pp. I-9, I-10, I-11 and I-12.

believes that for due process reasons the 1998 data used in its original filing should be relied upon in this case, to the extent that base year 1999 data are to be used, the Commission should rely upon base year 1999 First Class Mail cost estimates that incorporate the FY 1998 IOCS methodology. It is precisely these updated Library References LR-I-477 and LR-I-478 which were filed at such a late date by the Postal Service (August 25, 2000), that they have not been the subject of any written discovery, technical conferences, or even oral cross examination. Not a single witness has relied upon or adopted these updated Library References, and indeed the Postal Service in filing these Library References on August 25, 2000 clearly stated that its preference was not to rely on such updated Library References, but rather to use the base year 1998 data.<sup>2</sup>

As noted by ABA&NAPM at Pages 11-13 of their Initial Brief, these August 25, updated Library References LR-I-477 and LR-I-478, which utilize the 1998 IOCS methodology to measure cost avoidance of automated FCLM, result in a bizarre swing in cost avoidance figures, up 0.5 to 0.7 cents per piece from that which resulted from use of updated Library References LR-I-467 and LR-I-468 which had been filed one week earlier and which utilized a 1999 IOCS methodology. In the limited time (2-3 business days) in which ABA&NAPM witnesses Clifton and MMA witness Bentley had to review these Library References LR-I-477 and LR-I-478, they identified significant

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<sup>2</sup> Supplemental Response of United States Postal Service to Presiding Officer's Ruling No. 2000-1/116 (August 25, 2000).

aberrations and flaws.<sup>3</sup> Who knows what other errors might be contained in such updated Library References which would have been discovered had a reasonable period of time and even a minimum of discovery been allowed.

All of the due process concerns and potential for evidentiary flaws which the Postal Service correctly identified as flowing from incorporation of the FY 1999 CRA data are compounded by these August 25, 2000 updated Library References LR-I-477 and LR-I-478. To utilize such untested data which produce such a significant unexplained swing in cost avoidance, would be profoundly unfair to the Intervenor in this case.

If, notwithstanding the numerous shortcomings discussed above, the Commission determines that it will utilize not only the FY 1999 CRA data, but also the updated Postal Service Library References related thereto in order to measure cost avoidance, ABA&NAPM submit that the Commission should average the results of the August 25, 2000 updated Library References LR-I-477 and LR-I-478 (which utilize the 1998 IOCS methodology) with those resulting from the use of the August 18 and 21, 2000 updated Library References LR-I-467 and LR-I-468 (which utilize the 1999 IOCS methodology). ABA&NAPM witness Clifton suggested such a course, and indeed there is case support for the Commission choosing to "split the difference" when neither of two suggested adjustments applied to inaccurate data is completely satisfactory. The Association of American Publishers v. Governors of U.S. Postal Services, 485 F2d 768 at 773 (D.C. Cir. 1973).

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<sup>3</sup> Clifton Responsive Testimony (ABA&NAPM-ST-2) at Tr. Vol. 45, Page 20146 and August 29, 2000 Revised Supplemental Testimony of Bentley (MMA-ST-1) at Tr. Vol. 44, Pages 19081.

For the same reasons described above, ABA&NAPM oppose the suggestion made by the OCA at Page 17 of its Initial Brief that the Commission utilize even more recent data in the form of actual cost data collected and reported for FY 2000 in lieu of the FY 2000 Rollforward presented by witness Patelunas. It is not sufficient that cost data merely exist one nanosecond before the Commission issues its Recommended Opinion and Decision in a case. For any cost data to be a legitimate basis for a Commission rate decision, such cost data should have been presented in the case in a manner which has allowed the Postal Service and all intervenors the opportunity to evaluate such data, test the data through discovery and cross-examination, and comment to the Commission upon such data. The Commission should reject this suggestion of the OCA to rely upon actual FY 2000 cost data.

**III. By Any Fair And Reasonable Measure Automated FCLM Cost Avoidance Is increasing; Postal Service Cost Witness Miller himself admits that it is not shrinking.**

Workshare mailers have invested millions of dollars in the extremely successful Postal Service workshare program. The Commission must remain cognizant of the fact that there will always be a temptation for the Postal Service to offer narrow measurements of automated FCLM cost avoidance, taking the short term view that this may justify lower discounts which enable the Postal Service to retain an unfair amount of the true cost avoidance from the Workshare Program. In point of fact, to price automated FCLM discounts below the true value of such mail is not only unfair to workshare mailers, but is harmful to the Postal Service Workshare Program and the financial well-being of the Postal Service.

We submit that there are numerous indications in this case to support the conclusion that the Postal Services has consciously offered a narrow measurement of automated FCLM cost avoidance. These indications include the following:

1. The change to the CRA methodology itself - Faced with CRA figures which year after year demonstrated an increasing gap between the attributable cost of single piece FCLM and the attributable cost of presort FCLM, the Postal Service in 1997 made a methodological change to its CRA measurements by altogether eliminating the second largest traditional component in Cost Segment 3 of the CRA . . . mail processing overhead. This change, which had nothing to do with actual cost reduction, dropped total unit volume variable cost for First Class single piece mail from 26.1 cents per piece in 1996 to 21.8 cents per piece in 1997. The impact of this change on volume variable cost for First Class presort was less, and the result therefore was to understate cost avoidance between single piece FCM and presort FCM.<sup>4</sup>

2. USPS witness Miller's exclusion of cost pools previously utilized by the Postal Service - USPS Cost witness Miller (USPS-T-24) presented in this case a radically new costing methodology by creating and then excluding from the calculation of automated FCLM cost avoidance, a new category of "non-worksharing related" cost pools. This new methodology resulted in the exclusion of cost pools which USPS witnesses Hatfield and Smith had included in the automated FCLM cost avoidance equation in R97-1 and MC95-1 respectively.<sup>5</sup> Not only is Miller's exclusion of these cost pools contrary to prior USPS practices, but it is also counter-intuitive in that every

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<sup>4</sup> Clifton Direct Testimony (ABA&NAPM-T1) at Tr. Vol. 26, Page 12406.

significant cost pool which Miller excluded as unrelated to worksharing in fact contained a lower cost for worksharing mail than for BMM, thereby implying that such cost pools were very much related to worksharing.<sup>6</sup> ABA&NAPM witness Clifton in his calculation of automated FCLM cost avoidance adds back 12 of these 35 cost pools which were arbitrarily excluded by Miller. Dr. Clifton fully explains at Exhibit A to his Direct Testimony why each of such cost pools which he adds back is in fact related to workshare cost avoidance. The statement at Page VII-74 of the USPS Initial Brief that Dr. Clifton provides no task-based justification for adding back such pools is simply incorrect.<sup>7</sup>

3. Postal Service updated cost change factors in its Order No. 1294 filings were arbitrarily skewed in favor of Standard A Commercial Regular and single piece FCLM relative to automated FCLM - The Postal Service included in its updated cost change factors as part of its response to Commission Order No. 1294, subjective "break-through productivity" cost reduction initiatives which were based upon Postal Service Management budget projections and which were arbitrarily skewed in favor of single piece FCLM relative to automated FCLM, thereby resulting in a smaller measurement of automated FCLM cost avoidance.<sup>8</sup>

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<sup>5</sup> Id. at Page 12424 and 12426.

<sup>6</sup> Miller Direct Testimony (USPS-T-24) at Appendix I, Pages I-7, and I-9.

<sup>7</sup> See Clifton Direct Testimony at Tr. Vol. 26, Page 12473 (Exhibit A, Page 9).

<sup>8</sup> Clifton Revised and Updated Supplementary Testimony (ABA&NAPM-ST-1, Revised 8/23/00) at Tr. Vol. 45, Page 20093, Lines 5-21.

4. Phony BMM volume estimates - In order to support its argument for a bulk meter mail benchmark, which of course narrows the measurement of automated FCLM cost avoidance, Postal Service rebuttal witness Miller (USPS-RT-15) filed testimony actually claiming that the Postal Service did in fact receive large volumes of bulk metered mail. The clear implication of such testimony was that this mail was First Class mail delivered by mailers and was therefore candidate mail for conversion to automated FCLM. However, the Postal Service was caught red-handed with this ploy upon cross- examination when Mr. Miller was forced to admit that this supposed large volume of BMM mail included, in part, flats, standard mail, and, most importantly, mail delivered in single piece to the Postal Service, trayed by another Postal Service delivery unit, and then delivered to the appropriate Postal Service processing plant.<sup>9</sup> The lack of forthrightness on the part of the Postal Service on this issue should be taken by the Commission as evidence of the fact that the Postal Service is not offering objective measurements of automated FCLM cost avoidance.

5. Inclusion within Postal Service Initial Brief of cost avoidance calculations contradicted by Postal Service's own witnesses - Buried in the Postal Service brief at Page VII-77 is a legal argument made by the Postal Service lawyers, unsupported by any Postal Service witness, suggesting that automated FCLM cost avoidance may be dropping. In this portion of its Initial Brief, the Postal Service suggests that from 1997 to 1999 mail processing costs for BMM FCLM have dropped somewhat while mail processing costs for automation non-carrier route presort letters has increased

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<sup>9</sup> Miller Cross Examination at Tr. Vol. 45, Pages 19699, 19700 and 19702.

somewhat from 1998 to 1999. This is a most misleading argument which relies on inconsistent measures of cost avoidance and therefore fails to present any apples-to-apples comparison. In particular, for cost of BMM letters, the Postal Service lawyers take projections made by the Postal Service in R97-1 for the "test year (1997)" *sic*; they then compare this to a 1998 and 1999 base year cost which they derive from Library Reference I-81. Of course, the 1999 base year figure includes the effect of their subjective new cost change factors provided in response to Order No. 1294. The Postal Service lawyers then suggest that mail processing costs for FCLM automation non-carrier route presort letters has increased somewhat between 1998 and 1999 based upon Library Reference LR-1-81 in the case of 1998, and upon the infamous August 25, 2000 updated Library Reference LR-I-481 for 1999.

Noticeably absent from any of this discussion of the Postal Service lawyers is a cite to any Postal Service witness who would suggest that automated FCLM cost avoidance is shrinking. The obvious reason for this is that there is no Postal Service witness who has made or will make such a claim under oath. The data which the Postal Service lawyers use in their Initial Brief to support their suggestion of reduced automated FCLM cost avoidance is the very Order No. 1294 filings which they have spent 30 pages in the beginning of their Initial Brief correctly criticizing as being severely flawed and the product of improper due process. No Postal Service witness has adopted the Library References which they cite, and indeed the Postal Service lawyers in submitting such Library References have questioned the accuracy of such references.

There is one Postal Service witness in this case who has set forth his opinion under oath as to the direction of automated FCLM cost avoidance. That witness is Mr. Miller who in response to interrogatories was forced to admit the following:

"I do not have the view that cost avoidance is shrinking."<sup>10</sup>

6. Postal Service tries to ignore \$1.5 billion of move-update savings - Even stronger evidence of the fact that the Postal Service is offering a narrow measurement of automated FCLM cost avoidance is the refusal of the Postal Service to quantify and include move update savings within automated FCLM cost avoidance. Move update savings were forced upon workshare mailers in MC95-1 who objected to the burden of such requirements. But the Postal Service insisted upon such move update requirements (although it did not impose them upon single piece mail or bulk metered mail), because it wanted to recognize substantial savings in the form of reduced mail forwarding and return costs. The Postal Service has now been forced to acknowledge in this case \$1.5 billion in forwarding and return costs saved by it in FY 1998 as a result of the move update program.<sup>11</sup> Yet the Postal Service made no effort to include any of such \$1.5 billion in savings within its measurement of cost avoidance of automated FCLM.

The Commission should not allow the Postal Service to benefit from refusing, for the second major rate case in a row, to make any effort to include within its measure of automated FCLM cost avoidance the savings attributable to move update

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<sup>10</sup> Miller interrogatory response to ABA&NAPM/USPS-T24-26(b) at Tr. Vol. 7, Page 3071.

<sup>11</sup> Miller Cross Examination at Tr. Vol. 7, Page 3159, Line 20.

requirements. At the very least, the Commission should recognize this failure on the part of the Postal Service for what it is, which is yet additional evidence that the cost avoidance figures offered by the Postal Service in this case are extremely narrow and conservative.

ABA&NAPM respectfully submit that the most meaningful and accurate discussion of real trends in automated FCLM cost avoidance which has been presented in this case is that presented by Dr. Clifton in his Direct Testimony in which he demonstrated that from 1992 to 1999 there is a clear trend of increasing attributable cost differences between single piece and presort FCLM,<sup>12</sup> and that when compared on a true apples-to-apples basis, cost avoidance for automated basic, 3 digit and 5 digit FCLM is increasing from test year 1998 to test year 2001.<sup>13</sup> This detailed analysis of Dr. Clifton's was unrebutted by any USPS witnesses or any other witnesses, and unlike the unsworn economic arguments of Postal Service lawyers, can and should form a proper evidentiary basis for reasoned administrative decision-making by the Commission.

**IV. ABA&NAPM's Suggested Cost Coverage Adjustments Between First Class Mail And Standard Class Mail Are Fully Consistent With Statutory Pricing Factors, Commission Precedent And Sound Ratemaking Principles.**

ABA&NAPM witness Clifton suggested that part of the cost of the automated FCLM discounts proposed by ABA&NAPM could be covered by a modest increase in

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<sup>12</sup> Clifton Direct Testimony (ABA&NAPM-T1) at Tr. Vol. 26, Pages 12405-12412 (Figures 1, 2 and 3).

<sup>13</sup> Id. at Pages 12415 and 12416, Figures 4 and 5.

Standard A Commercial Mail rates. This increase, coupled with Dr. Clifton's proposed FCLM discounts and rates, would result in cost coverage for First Class Mail moving closer to the system-wide average and would narrow the gap between cost coverage of First Class Mail and Standard A Commercial Mail by moving both closer to the system-wide average. In making this proposal, Dr. Clifton correctly noted that to move the cost coverages for both First Class Mail and Standard A Commercial Mail in this direction was fully consistent with prior Commission precedent.<sup>14</sup>

Mail Order Association of America suggests in its Initial Brief that this position of Dr. Clifton is based upon a long-forgotten pronouncement of the Commission in R90-1 which was somehow mooted by the Commission in MC 95-1 when it denied subclass status to automated FCLM.<sup>15</sup> However, noticeably absent from the MOAA Initial Brief is any mention of the following pronouncement of the Commission in its MC95-1 opinion:

"The Commission has expressed its reluctance to shift too large a share of the total institutional cost burden to First Class in several recent omnibus rate cases [citations omitted] . . . The Commission's willingness to establish an additional subclass within Standard Mail should not be interpreted as a retreat from the view that the largest volume subclasses in First Class and Standard Mail should have roughly equivalent mark-up indices." PRC Op. MC95-1 ¶ 1019 (emphasis supplied).

Clearly, regardless of any subclass decisions made by the Commission in MC95-1, it did not abandon its longstanding view that cost coverage of First Class

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<sup>14</sup> Clifton Direct Testimony (ABA&NAPM-T1) at Tr. Vol. 26, Page 12458, Lines 13 and 14 and Page 12463, Lines 5-19. See PRC Opr 87-1, ¶ 4026; PRC Op R90-1, 4055; and PRC Op R94-1, ¶ 4041.

<sup>15</sup> See Initial Brief of MOAA at Page 15.

Letters and Standard A Commercial Mail should come closer together towards the system-wide average.

MOAA also suggests in its Initial Brief that because automated FCLM was denied subclass status in MC95-1, this somehow prevents adoption of Dr. Clifton's recommendations which would result in, *inter alia*, higher cost coverages for Standard A Commercial Regular and ECR and lower cost coverages for First Class Mail and for automated FCLM.<sup>16</sup> However, this position of MOAA ignores the fact that in order to bring the cost coverages of First-Class and Standard A mail closer together and closer to the system-wide average, the Commission will have to reduce the cost coverages of some, if not all, categories of First Class Mail and increase the cost coverages for some, if not all, categories of Standard Mail. It is perfectly appropriate for the Commission to narrow the gap in cost coverages between First-Class Mail and Standard Mail by making a modest decrease in automated FCLM rates and a modest increase in Standard A Regular and Standard A ECR rates. This is precisely what Dr. Clifton proposes.

Direct Marketing Association and Val-Pak/Carol Wright argue in their Initial Briefs that ABA&NAPM's proposed rates and discounts, which entail a modest reduction in the automated FCLM rates proposed by the Postal Service, and a modest increase in the Standard Commercial A Rates proposed by the Postal Service, fail to reflect consideration of the cost criteria of 39 USC § 3622(b) other than the first criteria of

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<sup>16</sup> MOAA Initial Brief at Page 15.

fairness and equity.<sup>17</sup> Both are incorrect in this regard. The modest adjustment in rates suggested by Dr. Clifton is supported not only by fairness and equity but also by the need to avoid the adverse effect which a reduction in automated FCLM discounts on an absolute basis would have upon workshare mailers [39 USC § 3622(b)(4)], the need to avoid the very real threat of electronic diversion of automated FCLM [39 USC § 3622(b)(5)], and the degree of preparation of automated FCLM and the resulting savings to the Postal Service [39 USC § 3622(b)(6)]. All of these factors were addressed by Dr. Clifton in his Direct Testimony.<sup>18</sup> We also submit that the value to the recipient of First Class Mail relative to Standard Commercial Mail [39 USC § 3622(b)(8)] supports the rates proposed by ABA&NAPM

Lastly, in their Initial Brief Val-Pak/Carol Wright offered the somewhat bizarre and counter-intuitive theory that because a competitive alternate delivery system for Standard A Commercial Mail could be established in the United States which would drain such mail from the Postal Service System, the magnanimous decision by Standard A Mailers to stay within the Postal Service System amounts to a "cross subsidization" of First Class Mail by Standard A Mail.<sup>19</sup> Apparently, Val-Pak/Carol

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<sup>17</sup> DMA Initial Brief at Pages 2-4; Val-Pak Direct Marketing Systems, Inc., Val-Pak Dealer's Association, Inc. and Carol Wright Promotions, Inc. Initial Brief at Pages 65-67.

<sup>18</sup> Clifton Direct Testimony (ABA&NAPM-T1) at Tr. Vol. 26, Pages 12402, 12403, 12434 and Pages 12468-12476.

<sup>19</sup> Val-Pak Direct Marketing Systems, Inc., Val-Pak Dealer's Association, Inc. and Carol Wright Promotions, Inc. Initial Brief at Pages 73-75. Val-Pak/Carol Wright's own witness on this issue, Dr. Haldi, acknowledged on cross examination the fact that Standard A Mail volume has continued to increase since 1994, notwithstanding rate increases during those years and that Standard A mail was price inelastic. Haldi Cross Examination Tr. Vol. 44 at Pages 18874 & 18876. See also L.R.-I-179, the GAO study which predicts continued Standard A Commercial Regular prebarcoded volumes

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Wright has adopted the strategy that the best defense is a good offense. Undaunted by the fact that First Class Mail would have 195% cost coverage compared to the 148% cost coverage of Standard A Commercial under the Postal Service proposal, or by the fact that this higher cost coverage will result in First Class Mail bearing a grossly disproportionate percentage of delivery costs relative to Standard A Mail (since nearly 49% of such delivery costs are treated as institutional),<sup>20</sup> Val-Pak/Carol Wright somehow believe that they can argue to the Commission that Standard A Mail subsidizes First Class mail delivery costs. Of course, this is ludicrous and should be taken by the Commission as nothing other than evidence of the weakness of the merits of the arguments of Standard Mailers that their cost coverages should not be moved closer to the system-wide average and closer to First Class Mail, as is proposed by ABA&NAPM.

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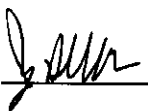
increasing in FY 2000 - FY 2008, notwithstanding rate increases and electronic divergence of advertising mail.

- 20 Clifton Direct Testimony at Tr. Vol. 26, Pages 12459 (Table Twelve), 12460, Lines 21-28, 12461 (Table Thirteen) and 12462 (Table Fourteen). Indeed if the Commission were to attribute a higher percentage of delivery costs than is proposed by the Postal Service, this would help to relieve the unfair burden of delivery costs being born by First Class Mail.

Respectfully submitted,

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NATIONAL ASSOCIATION OF PRESORT MAILERS

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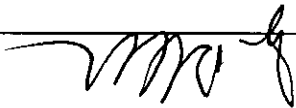
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**CERTIFICATE OF SERVICE**

I hereby certify that I have this date served the instant document on all participants of record in this proceeding in accordance with Section 12 of the Rules of Practice.

  
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September 22, 2000